Tuition Program -- "Recapture of Improper Distributions"

If a contribution that was previously deducted from Colorado taxable income under the Colorado tuition program contribution subtraction is withdrawn from the account for a use other than paying higher education costs of the account beneficiary, is the amount withdrawn subject to Colorado tax in that year?

Yes. The principal amount of any money deposited into a qualified state tuition program is generally not taxable when withdrawn or distributed. However, the withdrawal or distribution will be taxable in the year withdrawal if:

- 1. you previously deducted the payments or contributions on a Colorado income tax return, and
- 2. the withdrawal is not made for one of the following purposes:
- To pay qualified higher education expenses (as defined in section 529(e)(3) of the Internal Revenue Code),
- As a result of the beneficiary's death or disability, or
- As a result of receiving a scholarship and as long as the amount of distribution, refunds, or withdrawals made do not exceed the amount of the scholarship provided during such tax year.

The amount of any taxable withdrawal or distribution must be added to taxable income on Form 104 on the "Other additions" line in the year the distribution is received.

Similarly, if you use these funds to pay the education expenses of someone other than the designated beneficiary, the funds become taxable in Colorado -- even if the expenses otherwise qualify as higher educational expenses.